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State treasurer, ASU professor say feds to blame for bailout

The federal government has nobody but itself to blame for the firestorm that surrounds the $700 billion Wall Street rescue plan, according to Arizona State Treasurer Dean Martin.

Martin said the feds made a mistake when, after bailing out Bear Stearns investment bank, they refused to provide emergency lending to Lehman Brothers.

"That set the market ablaze," he said.

Then -- with the bailouts of AIG, Fannie Mae and Freddie Mac -- the government started moving the goalposts, based on whether the feds liked a company and its leaders, said Martin. . That caused the markets to lose all confidence.

"If they would go back and say, 'Oops, we made a mistake. We need to make good on that original promise, pull Lehman back from bankruptcy,' they no longer would need to bail out AIG, because AIG was taken down by Lehman," Martin said.

He said the bailouts of AIG, Fannie and Freddie created a very dangerous precedent.

"Once you're willing to bail out and buy out an insurance company, what stops you from an auto maker or the next company? The moral hazard has been set aside."

The bailouts were a bad idea, in general, Martin said.

"When your neighbor's house is on fire, you'll lend them a water hose to help them put it out. You don't make him sign over a deed to his house before you help him fight the fire. And it seems like they're going down that road."

Martin believes the United States is the closest it's been to a meltdown since the Great Depression of the 1930s.

``This isn't just a mild economic cycle, this is much more serious," he said.

But, he doesn't think it will get quite as bad as the 1930s.

"We learn from some of the mistakes from the Great Depression. We obviously haven't learned them all because we're in a situation where we could head down that road. I don't think we're going to be there."

The bailout of AIG caused Martin to adjust his views of when the economic downturn will end.

"I was predicting that we would start our recovery at the beginning of next year," he said, "But, it's at least six months, or more behind."

The federal government used to be the lender of last resort, but that's all changed now, Martin said, adding he fears where that might lead.

"In a year or two, we start anything up, something like between the U.S. and Soviet Union, where the government runs half of industry? The last thing I want is FEMA running my local bank."

Professor Anthony Sanders of the W.P. Carey School of Business at Arizona State University agrees with Martin that the government in essence caused its own problems. He said the banks with bad loans on the books could have sold them, but not for the price they wanted.

"So the federal government's going to step in and pay the banks the price they want?" he asked. "That's a bailout of the banks, so in a sense that's not right."

People who got subprime loans got them for a reason, he said, "meaning that they should not have gotten credit. They government interfered and encouraged them to take out credit. They defaulted in large numbers, so now we're left with a mess."

"The people who are speculating in the housing market are getting off scot-free, and the banks that had crummy underwriting standards are kind of getting off scot-free, too," Sanders said.

He added, "The price tag is going to destroy our economy. We've got to get off it and return to more personal responsibility and less government involvement because they did not act responsibly. They put us in the position that we're in today."

He said the bailout "is a gamble. There's nothing carved in stone that this is going to work. It's an attempt at making something work."

If it does work, it would be "phenomenal," he said.

Could the bailout cause a depression?

"Sure, absolutely, there's no doubt that it could lead to that," Sanders said.

by Jim Cross/KTAR